

**ASSESSMENT OF COMPETITION IN THE ILLINOIS ELECTRIC  
INDUSTRY IN 2002**

**ILLINOIS COMMERCE COMMISSION**

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## **Executive Summary**

Sec. 16-120(b) of the Public Utilities Act (“Act”) directs the Illinois Commerce Commission (“Commission”) to submit an annual report to the Joint Committee on Legislative Support Services of the General Assembly and the Governor that provides information concerning the development of competitive electricity markets in Illinois. This is the third report the Commission has submitted to the General Assembly pursuant to this section of the Act. The Commission recently submitted a pursuant to Sec. 16-120(a) report to the General Assembly on the topic of electric competition in Illinois retail and wholesale electric markets. That report is broader in scope than this report, and contains legislative recommendations for addressing problems that have hindered the growth of competition in Illinois electric markets.<sup>1</sup>

Sec. 16-120(b) requires the Commission to furnish certain statistical information concerning power and energy sales by electric utilities and also by Alternative Retail Electric Suppliers (“ARES”) to customers eligible to select new suppliers. The Commission may also provide any other information the Commission believes is relevant in assessing the development of Illinois electricity markets.

The Sec. 16-120(b) reports will continue to 2006. The series of reports will thus consider developments in the Illinois electric industry occurring during the “transition period,” during which the State’s electric utilities are expected to increase efficiency and reduce costs in preparation for the period, beginning as early as 2007, when they will no longer be permitted to charge transition charges to customers who choose alternative suppliers.

### **Retail Market Activities**

The electric market opened in October 1999 to approximately one-third of all non-residential customers, comprising a total of about 64,000 customers. On January 1, 2001, all non-residential customers of the investor-owned utilities became eligible for delivery services. The number of eligible non-residential customers (excluding street lighting customers) is now about 500,000. An additional 4,440,000 residential customers became eligible for delivery services in May 2002.

### **Supply Options Available to Delivery Services Customers**

Customers eligible for delivery services have several supply options available to them from both the incumbent utilities and the alternative suppliers. Customers may purchase bundled power and energy offered by the incumbent utilities at rates regulated by the Commission. These rates are frozen until 2007. In addition, both prior

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<sup>1</sup> Please refer to the Electricity page of the Commission’s web site at <http://www.icc.state.il.us/ec/electricity.aspx>.

to the 1997 restructuring law and subsequent to the enactment of the restructuring law, some utilities have offered discounted bundled rate contracts to customers.

Customers may also choose to purchase power and energy on an “unbundled” basis, by switching the generation portion of their electric service to an ARES or from any electric utility serving outside its traditional service area. (Collectively, the ARES and electric utilities serving outside their service areas are called “Retail Electric Suppliers” or “RESs”). Some utilities also offer an unbundled, market-based generation option called the “Power Purchase Option” (“PPO”). As described in Section 16-110 of the Act, non-residential customers subject to transition charges must be offered PPO service. Currently, only two utilities (Commonwealth Edison and Illinois Power) charge transition charges to customers who receive delivery services. Unbundled power and energy, whether purchased from an ARES, or from an electric utility under the PPO, is delivered to customers under “delivery services tariffs” at rates regulated by the Commission.

Approximately 23,350 non-residential customers were taking delivery services customers at the end of 2002. About 21,550 ComEd customers, or about 6.5% of ComEd’s non-residential customers, had selected delivery services. The other 1,800 delivery services customers are located in the service territories of AmerenCIPS and Illinois Power, where about 1.6% of each company’s non-residential customers had selected delivery services by the end of 2002.<sup>2</sup> More suppliers made sales in these two downstate service territories in 2002 than in 2001. New switching activity may be expected in the AmerenCIPS service territory, as AmerenCIPS has suspended its collection of transition charges for at least two years, starting in mid-2003.<sup>3</sup>

#### Retail Electric Supplier Activities

Twelve RESs sold power and energy to retail customers in 2002. One RES was certified in 2002, and one RES requested decertification from the Commission. RESs made sales in 2002 of about 16.3 million megawatt-hours (“mWh”). This total represents about 12.5% of sales to all retail customers. There was no indication by the end of 2002 that RESs were actively marketing in any of the State’s six smallest service areas or were interested in marketing power to residential customers.

#### Power Purchase Option Sales

In 2002, over 40% of the unbundled power and energy sales were PPO sales. The PPO is especially popular in the Illinois Power service area, where 99% of delivery services customers with a demand under one megawatt (“MW”) were taking service under the PPO. The Commission has noted in prior reports that reliance on the PPO may be cause for concern for the long-term development of the market, primarily

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<sup>2</sup> These percentages exclude about 250,000 very small-use customers, such as streetlighting customers.

<sup>3</sup> See Docket No. 02-0657.

because of the temporary nature of the PPO. Electric utilities will cease offering the PPO by the end of 2006, when the statutory “Mandatory Transition Period” terminates.<sup>4</sup>

### **Peak Demand and Sales**

The sum of the non-coincident peak demands of the nine investor-owned utilities totaled 29,648 megawatts. This total, which encompasses both unbundled and bundled customer demand, represents an increase in peak demand of approximately 0.6%, compared to 2001. Non-coincident peak demand grew at an annual growth rate of about 1.6% between 1991-2002, an increase of about 439 megawatts per year.

### **Wholesale Market Activities**

The ultimate success of electric restructuring depends to a great extent on the competitiveness of the wholesale market. The competitiveness of the wholesale market will also greatly influence the electricity prices for both unbundled and bundled customers. Since the State’s largest utilities have transferred or sold their generating facilities, the power and energy needed to serve their retail customers must be purchased from merchant generators in the wholesale market. Currently, these utilities have wholesale power contracts in place with the companies that now own the generating facilities, but these contracts will expire by January 1, 2007, just as the retail rate freeze expires.

While wholesale prices have dropped considerably over the past two years, it is unknown how this price decrease will affect the prices utilities pay for power deliveries that begin in 2007. It may also be too early to predict whether the power prices retail customers will pay in 2007 and later years will be higher than the prices they are currently paying. However, the Commission is concerned that the wholesale market is not sufficiently competitive to ensure that wholesale prices remain at reasonable levels.

The Commission’s evaluation of the competitiveness of the wholesale market is described in the Commission’s most recent Sec. 16-120(a) report.

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<sup>4</sup> See Sec. 16-102 of the Public Utilities Act.

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## **I. Introduction**

Sec. 16-120(b) of the Public Utilities Act requires the Illinois Commerce Commission to submit an annual report to the Joint Committee on Legislative Support Services of the General Assembly and the Governor describing the development of electric competition in Illinois. Sec. 16-120(b) requires the Commission to furnish certain statistical information related to sales by electric utilities, both inside and outside their service territories, as well as sales by Alternative Retail Electric Suppliers (“ARES”). This statistical information required by statute is supplemented with other statistical information to illuminate the extent of competition in Illinois retail electric markets.

An examination of the switching statistics provided in the report shows indications of retail electric market growth in the service territories of the three largest utilities in the state. In the Commonwealth Edison (“ComEd”) service territory, a relatively large and growing number of customers have switched from ComEd’s basic bundled service to delivery services, continuing a growth pattern that began as soon as the market opened to electric customers in October 1999. By the end of 2002, over 21,500 ComEd customers had switched either to alternative supplier or to the Power Purchase Option (“PPO”), a market-based service that is available only to the customers of the utilities that assess transition charges.

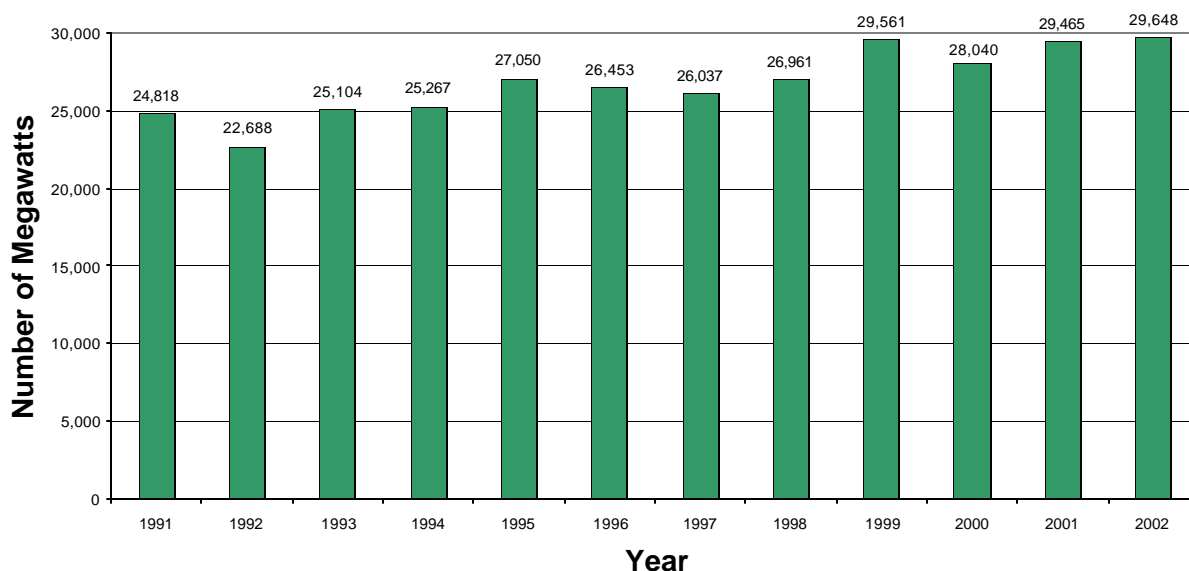
Customer switching is nearing or has surpassed the 1,000 customer mark in the service territories of AmerenCIPS and Illinois Power, the two other utilities that charge transition fees and thus offer the PPO as an alternative to bundled service. However, customer switching has been virtually non-existent in the service territories of the state’s smaller utilities. After over three years of the availability of delivery services, there are few signs that customers in those service areas will have supply options other than the bundled service offering provided by the utilities when the restructuring law was enacted in late 1997.

## **II. Peak Demand and Sales by Electric Utilities and ARES**

Figure 1 shows the level of non-coincident peak demand of the State’s nine investor-owned utilities between 1991 and 2002. Non-coincident peak demand in Illinois has grown at an annual rate of about 1.6% since 1991.



**Figure 1: Illinois Investor-Owned Electric Utility Non-Coincident Peak Demand, 1991-2002 (MW)**



#### **A. Electric Sales By Electric Utilities and ARES**

Sec. 16-120(b)(2) requires the Commission to collect data concerning the following:

the total annual kilowatt-hours delivered and sold to retail customers in the State of Illinois by each electric utility within its service territory, each electric utility outside its service territory, and alternative retail electric suppliers in the preceding calendar year.

Sec. 16-120(b)(3) requires the Commission to express the information collected in response to Sec. 16-120(b)(2) in percentage terms. Together, these two subsections provide an indication of the marketing success alternative suppliers have achieved since the retail market opened in October 1999.

The Commission gathered information from the utilities and ARES concerning their electricity sales to retail customers during 2002. This information is summarized in Table 1. (For comparison purposes, data from 2001 is shown Table 2.) Total sales by electric utilities include the following: (a) bundled electricity sales; (b) “Contract Sales,” which include sales under Sec. 16-106 and Sec. 16-116 of the Act, sales under “special rate contracts” that were entered into prior to the December 1997 enactment of the 1997 restructuring law, sales to delivery services customers under the incumbent

utilities' delivery services tariffs and sales under "Interim Supply Service";<sup>5</sup> (c) PPO sales, including both "unassigned" and "assigned" sales; and (d) sales by electric utilities outside their service territories. The sales by ARES are electric sales to delivery services customers under the incumbent utilities' delivery services tariffs. The sales by electric utilities plus sales by ARES equal "deliveries."

Table 2 shows that by the end of 2002 the ARES had obtained a growing fraction of the customers eligible for delivery services. Overall sales to retail customers grew about 0.5% from 2002. Sales to all retail customers, including delivery services customers, totaled approximately 130.4 million mWh during 2002; the ARES' shares of these sales were about 9.7 million mWh, or 7.4% of all sales. Sales by utilities operating outside their service territories (AmerenCILCO, AmerenCIPS, Illinois Power and MidAmerican) were approximately 6.6 million mWh, or 5.0% of all sales. Thus, sales by RESs equaled about 12.5% of all sales. This percentage represents about a 36% increase from 2002, when RESs obtained sales of about 9.1% of all retail sales. Part of the reason for the increase appears to be that RESs gained sales to customers that were formerly served by utilities under various types of contracts. Contract sales dropped by almost one-half, compared to 2002.

**Table 1: Sales by Electric Utilities and ARES During 2001<sup>6</sup>**

<i><b>Sellers</b></i>	<i><b>Electric Utilities</b></i>				<i><b>ARES</b></i>
<i><b>Sales Category</b></i>	<i><b>Bundled</b></i>	<i><b>Contract</b></i>	<i><b>PPO</b></i>	<i><b>Outside Territory</b></i>	<i><b>Retail</b></i>
<i><b>Amount of Sales (Million mWh)</b></i>	94.1	13.2	10.7	5.4	6.4
<i><b>Percent of All Sales</b></i>	72.5	10.1	8.2	4.2	4.9

**Table 2: Sales by Electric Utilities and ARES During 2002**

<i><b>Sellers</b></i>	<i><b>Electric Utilities</b></i>				<i><b>ARES</b></i>
<i><b>Sales Category</b></i>	<i><b>Bundled</b></i>	<i><b>Contract</b></i>	<i><b>PPO</b></i>	<i><b>Outside Territory</b></i>	<i><b>Retail</b></i>
<i><b>Amount of Sales (Million mWh)</b></i>	94.7	7.3	12.1	6.6	9.7
<i><b>Percent of All Sales</b></i>	72.7	5.6	9.3	5.0	7.4

<sup>5</sup> Interim Supply Service is a tariffed short-term service available to delivery services customers who have no source of electric supply.

<sup>6</sup> Electric utilities and ARES provided the data in Tables 1 and 2.

### III. Customer Switching Activity in 2002

In this section the Commission examines various indicators of the development of a retail electric market in Illinois. Customer switching statistics are presented below in Tables 3-6 for the State's six largest utilities. Customer selection of the Power Purchase Option is discussed in Section III.B. Supplier activity is discussed in Section III.C.

#### A. Delivery Services Growth

Customer switching rates, as measured by customer movement from bundled service to delivery services, continue to be high in the ComEd region relative to other service territories. As shown in Table 3, about 21,500 ComEd customers have now switched to delivery services. Particularly notable is the fact that about 60% of customers with demand of greater than one megawatt have made the decision to switch from bundled service to delivery services.

Table 3 also shows that about 6% of smaller-use ComEd customers have switched to delivery services, a figure that seems greatly reduced from last year's 21% figure. Perhaps a more relevant statistic is the amount of customer load that has switched to delivery services (Table 4). These percentages (26% for smaller customers and 57% for larger customers) indicate that a significant amount of non-residential customer usage has switched to delivery services in the ComEd area.

Customer switching activity is growing more slowly in the AmerenCIPS and Illinois Power service territories, the only other areas in which customers switched to delivery services during 2002. About 750-1,000, relatively large customers in these two service territories have switched to delivery services.

**Table 3: Number of Delivery Services Customers in 2002**

<i>Utility / Demand Level</i>	<i>Number of Customers Eligible for Delivery Services</i>		<i>Number of Customers Switched to Delivery Services</i>		<i>Percentage of Customers Switched to Delivery Services (%)</i>	
	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>
<b>AmerenCILCO</b>	19,935	71	0	0	0.0	0.0
<b>AmerenCIPS</b>	47,338	119	703	44	0.0	0.0
<b>AmerenUE</b>	7,504	40	0	0	1.5	37.0
<b>ComEd</b>	328,038	1,846	20,465	1,101	6.2	59.6
<b>Illinois Power</b>	65,986	218	990	61	1.5	28.0
<b>MidAmerican</b>	1,392	28	0	0	0.0	0.0
<b>Total</b>	470,193	2,322	22,158	1,206	4.7	51.9



**Table 4: Amount of Usage Switched to Delivery Services in 2002**

<i>Utility / Demand Level</i>	<i>Amount of Usage Eligible for Delivery Services (Thousand mWh)</i>		<i>Amount of Usage Switched to Delivery Services (Thousand mWh)</i>		<i>Percentage of Usage Switched to Delivery Services (%)</i>	
	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>
<b>AmerenCILCO</b>	2,293.6	1,713.4	0.0	0.0	0.0	0.0
<b>AmerenCIPS</b>	2,399.6	2,922.8	300.3	1,161.4	0.0	0.0
<b>AmerenUE</b>	661.7	1,981.4	0.0	0.0	12.5	39.7
<b>ComEd</b>	31,230.2	26,825.8	8,083.7	15,153.8	25.9	56.5
<b>Illinois Power</b>	4,678.8	8,285.9	681.5	4,424.9	14.6	53.4
<b>MidAmerican</b>	484.6	370.6	0.0	0.0	0.0	0.0
<b>Total</b>	41,748.5	42,099.9	9,065.5	20,740.1	21.7	49.3

**B. Power Purchase Option**

Tables 5 and 6 show that over 40% of ComEd's delivery services customers have switched to the PPO, a figure that is consistent with switching trends in the ComEd service area over the last few years. In the AmerenCIPS and Illinois Power service areas, the PPO percentages are even larger. The PPO is the most popular delivery service offering in the AmerenCIPS area, as about 75% of AmerenCIPS' delivery services customers have switched to PPO service. Almost 99% of Illinois Power delivery services customers under one MW were taking PPO service at the end of 2002, and about 80% of IP's larger-use delivery services customers have switched to the PPO.

The Commission has noted in previous Sec. 16-120 reports that the popularity of PPO service can be viewed as an unfavorable sign of the prospects for the long-term development of a competitive retail market. From one viewpoint, the existence of the PPO allows customers to receive a rate discount even when no suppliers are serving the market. The PPO also allows suppliers to gain a market foothold and establish customer relationships because suppliers can essentially resell the utility's PPO to customers, either as a "billing agent" or through the "PPO Assignment" provisions of Section 16-110 of the Act. On the other hand, suppliers and customers can rely on PPO service only until the end of 2006. It is also possible that the PPO will vanish as a supply option prior to 2006 if a utility voluntarily forgoes the collection of transition charges or if customer transition charges equal zero, as the Ameren companies have proposed. Once the PPO ceases to be a service offering, the customers who have found the PPO a convenient way to receive a rate discount without having to take a step into the market may well discover that they have to return to the higher-priced bundled service, unless they are fortunate enough to find a RES who is willing and able to offer a competitive price. Moreover, there is no guarantee that traditional bundled service

will always be available to customers, as provisions in the Act permit utilities to petition the Commission to declare power and energy competitive, which could result in utilities dropping bundled service for some customers.<sup>7</sup>

**Table 5: Selection of Power Purchase Option During 2002**

<i>Utility / Demand Level</i>	<i>Number of Customers Switched to Delivery Services</i>		<i>Number of Customers Selecting Power Purchase Option</i>		<i>Percentage of Delivery Services Customers on Power Purchase Option (%)</i>	
	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>
<b>AmerenCIPS</b>	703	44	530	24	75.4	54.5
<b>ComEd</b>	20,465	1,101	8,551	508	41.8	46.1
<b>Illinois Power</b>	990	61	984	49	99.4	80.3
<b>Total</b>	22,158	1,206	10,065	581	45.4	48.2

**Table 6: Amount of Usage Switched to the Power Purchase Option During 2002**

<i>Utility / Demand Level</i>	<i>Amount of Usage Switched to Delivery Services</i>		<i>Amount of Usage Switched to Power Purchase Option</i>		<i>Percentage of Delivery Services Usage on Power Purchase Option (%)</i>	
	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>
<b>AmerenCIPS</b>	300.3	1,161.4	264.3	424.8	88.0	36.6
<b>ComEd</b>	8,083.7	15,153.8	2,826.3	6,847.3	35.0	45.2
<b>Illinois Power</b>	681.5	4,424.9	674.2	1,936.4	98.9	43.8
<b>Total</b>	9,065.5	20,740.1	3,764.8	9,208.5	41.5	44.4

### **C. Retail Electric Supplier (“RES”) Activity**

Twelve suppliers, either certificated suppliers or electric utilities serving outside their home service areas, sold power and energy to retail customers in 2002. The list of suppliers is comprised of Alternative Retail Electric Suppliers, which must obtain a certificate from the Commission before serving customers, and electric utilities serving outside their service areas. These entities are collectively known as “Retail Electric Suppliers.” With three exceptions, each RES that made retail sales in 2002 is either an Illinois utility or an affiliate of an Illinois gas and/or electric utility. Other suppliers may have participated in the market by marketing the utility’s PPO. About 15 RESs are permitted to sell power and energy to retail electric customers in Illinois.

<sup>7</sup> In its Order in Docket No. 02-0479, the Commission permitted ComEd to designate customers with a demand exceeding 3 MW as a competitive customer class.

Most suppliers are concentrating their marketing efforts in the ComEd service territory. As shown in Table 7, eight suppliers sold power and energy (or took part in a PPO Assignment transaction) in the ComEd service territory during 2002, one more than in 2001.

Four suppliers accumulated almost 90% of all RES sales to ComEd customers. In 2001, only three suppliers had obtained that level of retail sales, perhaps indicating that competition among RESs is increasing in the ComEd service area. Five different suppliers sold power and energy to downstate customers, two more than in 2001. The number of suppliers in the downstate areas is slowing increasing from previous levels.

**Table 7: Number of Active Retail Electric Suppliers During 2000, 2001, and 2002, by Service Territory**

<b>Electric Utility Service Area</b>	<b>Number of Active RESs in 2000</b>	<b>Number of Active RESs in 2001</b>	<b>Number of Active RESs in 2002</b>
<b>AmerenCIPS</b>	3	2	4
<b>AmerenUE</b>	1	0	0
<b>ComEd</b>	8	7	8
<b>Illinois Power</b>	4	3	4
<b>MidAmerican</b>	1	1	0
<b>All Others</b>	0	0	0

#### **D. Residential Market Activities in 2002**

The Commission has not received any applications for certification to serve the approximately 4.4 million eligible residential customers. Suppliers have cited relatively high transactions costs as one reason why they may not direct their marketing efforts towards residential customers, at least in the near term. In particular, the cost of marketing to small-use, individual customers is high compared to the potential profit margin that a supplier might expect to receive by serving a residential customer. The Commission has attempted to address the problem of supplier transaction costs through its consideration of pending rule 83 Illinois Administrative Code Part 453 "Internet Enrollment Rules."<sup>8</sup> If adopted, this rule would enable electric suppliers to use their Internet web sites to enroll customers, a procedure commonly used by suppliers in other industries in an effort to minimize transaction costs.

Another reason why the residential market may not be attractive to suppliers at the current time is that utilities do not offer the PPO to residential customers. Those suppliers that use the PPO as a primary supply resource will need to find other

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<sup>8</sup> See Docket No. 02-0290.

sources of supply if they intend to serve residential customers. It is uncertain whether more than a limited number of residential suppliers will be willing to rely on the wholesale market for their supply, at least at the present.

Finally, the residential rate decreases required by the restructuring law, which now total 20% for ComEd and IP residential customers, have brought electric prices for the customers of these two utilities closer to the rates paid by customers elsewhere in Illinois and the Midwest. Suppliers may find it easier to interest customers in switching away from bundled service after the expiration of the rate freeze in 2007, when prices may rise from current levels.

#### **IV. Conclusion**

In some service territories of the state, a fairly significant number of customers are taking advantage of the opportunity to reduce their electric costs. In particular, a large percentage of high-use customers are switching to either a lower-cost service generation service offered by the incumbent utilities or to services provided by Retail Electric Suppliers.

However, there are a number of problems facing the development of healthy competition for retail electric power in Illinois. With respect to the retail market, about 40% of the customers who have switched to delivery services have switched to the Power Purchase Option rather than to a supplier who is purchasing power on the wholesale market for resale to retail customers. From a long-run perspective, customer reliance on the PPO as a strategy to save money is worrisome because the PPO will only be available to customers through the end of 2006. Other problems in the retail market include a lack of interest among suppliers in serving residential customers and non-residential customers in the service areas of the State's smallest utilities.

Problems in the wholesale market include affiliate ownership of generation, limited transmission capability and high market concentrations in generation ownership. Since most electric utilities will purchase from the wholesale market much of the power they need for their bundled customers in 2007 and beyond, problems in the wholesale market will create problems in the retail market as soon as 2007, when the existing rate freeze expires. Wholesale market development issues are more fully discussed in the Commission's recent Sec. 16-120(a) report to the General Assembly. Also contained within that report are a number of legislative recommendations that the Commission believes would enhance the prospects for a competitive wholesale market.